

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

BOONESBORO WATER ASSOCIATION, INC.)
(1) FOR APPROVAL OF THE INCREASED)
RATES PROPOSED TO BE CHARGED BY THE) CASE NO. 9312
ASSOCIATION TO THE CUSTOMERS OF THE)
ASSOCIATION; (2) APPROVAL OF THE)
RULES AND REGULATIONS)

O R D E R

On March 28, 1985, Boonesboro Water Association, Inc., ("Boonesboro") filed an application with the Commission for approval of the following: an increase in the rates Boonesboro could charge both its water utility ("Boonesboro Water") and sewer utility ("Boonesboro Sewer") and its proposed rules and regulations.

A hearing on Boonesboro's proposed rate increase and rules and regulations was held on October 24, 1985. There were no intervenors and no protests were entered.

Boonesboro requested rates which would produce annual increases of \$42,000 for Boonesboro Water and \$3,444 for the Boonesboro Sewer. In this Order the Commission has allowed rates which will produce annual increases of \$29,985 for Boonesboro Water and the entire requested amount of \$3,444 for the Boonesboro Sewer.

COMMENTARY

Hearing

Throughout this proceeding the Commission has shown its concern for Boonesboro's accounting procedures and billing analysis. This concern was made evident in the two information requests which were issued prior to the hearing. However, at the hearing Boonesboro's witnesses could not properly answer the Commission's questions. This necessitated the need for the Commission to request additional information to be filed after the hearing which caused the procedure to be unduly delayed. Therefore, the Commission advises Boonesboro that its witnesses should be adequately prepared in any future proceeding in order to help expedite the process.

Allocation of Expenses

Boonesboro stated in response to the initial information request that the only expenses incurred by Boonesboro Sewer were for maintenance and depreciation.¹ However, in response to the second information request Boonesboro explained that it had never attempted an apportionment of the expenses which were common to the operation of both utilities, but if such an apportionment was made then it should be calculated according to the revenues generated from both utilities.²

At the hearing the Honorable David B. Redwine, attorney for Boonesboro, stated that Boonesboro Water subsidized the operation

¹ Item No. 6 of information request dated May 16, 1985.

² Item No. 6 of information request dated July 26, 1985.

of Boonesboro Sewer.³ This results in cross-subsidization of the utilities and causes the Boonesboro Water customers to contribute to the operation of Boonesboro Sewer from which they receive no benefits. The proper way to alleviate this unfairness would be an apportionment of the common expenses which would assure that the Boonesboro Sewer customers pay for the service they receive. The Commission is unable to calculate an apportionment of the expenses at this time due to inadequate information and the lack of knowledgeable witnesses at the hearing. Further, taking into consideration the large differences in the customer bases and operating costs of the two utilities, the effects of cross-subsidization on a per customer basis is minimized. The Commission does, however, advise Boonesboro that it should in future proceedings and/or by the 1985 Annual Report attempt to apportion the common expenses incurred in the operation of both utilities and where possible use actual figures.

TEST PERIOD

Boonesboro has proposed and the Commission has accepted the 12-month period ending December 31, 1984, as the test period in this matter.

BOONESBORO WATER REVENUES AND EXPENSES

Boonesboro Water had a net operating income in the amount of \$3,330 for the test period. The only adjustment proposed by

³ Transcript of Evidence ("T.E.") dated October 24, 1985, page 7.

Boonesboro Water was to the purchased water expense which results in an adjusted test period operating loss in the amount of \$27,670. The Commission has made the following adjustments to expenses, in conformance with its rate-making practices to more fairly represent the actual operating expenses of Boonesboro Water:

Depreciation Expense

Boonesboro's test period depreciation expense was \$17,027, which reflects depreciation on total plant using a composite rate of approximately 2.49 percent.⁴ The Commission's practice is to compute depreciation expense for rate-making purposes on the basis of original cost of the plant in service less contributions in aid of construction. The balance sheet filed by Boonesboro shows contributions in aid of construction at the end of the test period to be \$95,570. This amount is approximately 14 percent of the total cost of the utility plant in service. In determining the pro forma depreciation expense the Commission has utilized the depreciation rate applied by Boonesboro and excluded depreciation associated with contributed property. The adjusted depreciation expense for rate-making purposes is \$14,669,⁵ a reduction of \$2,358.

⁴ $\$17,027 \div \$683,547 = 2.49\%$.

⁵

Total Plant	\$684,675
Less: Contributions in aid of construction	95,576
Non-contributed Plant	<u>\$589,099</u>
Times: Composite Rate	2.49%
Depreciation Allowed for Rate-making Purposes	<u>\$ 14,669</u>

Purchased Water

Boonesboro's test period water purchases and sales were 122,382,000 gallons and 95,034,570 gallons, respectively. This reflects water loss of 22.34 percent, which is in excess of the maximum of 15 percent allowed by the Commission for rate-making purposes. Thus, the Commission has determined the allowable gallons of purchased water for rate-making purposes to be 111,805,376 gallons.⁶ This results in a test-period allowable purchased water expense of \$125,557,⁷ and reflects a decrease of \$27,866 from Boonesboro's adjusted level.

Therefore, the Commission finds that Boonesboro Water utility's adjusted test period operations are as follows:

	Boonesboro Water's Proposed Adjusted	Commission Adjustments	Commission Adjusted
Operating Revenues	\$216,101	-0-	\$216,101
Operating Expenses	257,960	\$<30,224>	227,736
Operating Income	<u>\$<41,859></u>	<u>\$ 30,224</u>	<u>\$<11,635></u>

BOONESBORO WATER'S REVENUE REQUIREMENTS

Boonesboro's annual debt service based on debt outstanding during the test period is \$29,404.⁸ Boonesboro's adjusted net

⁶ 95,034,570 gallons (Water Sold) ÷ 0.85 = 111,805,376 gallons.

⁷ (111,805,376 gallons ÷ 7.48 gallons/cu. ft.) X \$.84/100 cubic feet (Cost at New Rate) = \$125,557

⁸ Bonds (5-year average principle 1986-90) \$10,872
Interest (5-year average 1986-90) 18,532
Annual Average Debt Service \$29,404

operating loss of \$11,635 plus interest income from operations of \$14,189 provides a debt service coverage (DSC") of 0.09X. To achieve a DSC of 1.2X, which the Commission is of the opinion is the fair, just and reasonable coverage necessary for Boonesboro to pay its operating expenses and to meet the requirements of its lenders, Boonesboro would require a net operating income of \$35,285. Accordingly, the Commission has determined that additional revenue of \$32,731 is necessary to provide the 1.2X DSC which will ensure the financial stability of Boonesboro.

BOONESBORO SEWER
REVENUES AND EXPENSES

Boonesboro incurred an actual operating loss in the amount of \$2,276⁹ for the test period. Boonesboro Sewer proposed no adjustments to its test period revenues and expenses and the Commission has accepted Boonesboro Sewer's actual revenues and expenses as presented.

BOONESBORO SEWER
REVENUE REQUIREMENTS

The Commission has used the operating ratio method as the basis in determining sewer rates in the past and has found it to be a fair method to both the utility and its customers. The increased revenues proposed by Boonesboro Sewer results in an operating ratio of 90 percent. The Commission is of the opinion that this ratio is fair, just and reasonable in that it will

⁹ Operating Revenue
 Operating Expenses
 Operating Loss

\$ 8,065
10,341
\$ <2,276>

enable Boonesboro Sewer to pay its operating expenses and provide an adequate debt service coverage. Therefore, the Commission finds that Boonesboro Sewer is entitled to adjust its rates to produce total revenues of \$11,751. This results in an annual increase in revenue to Boonesboro Sewer of \$3,444 over test period actual revenue of \$8,065.

TARIFF AND RATE DESIGN

Boonesboro provides water service to approximately 836 customers and sewer service to approximately 72 customers. All customers who receive sewer service from Boonesboro are also provided water service.

Water Rates

Boonesboro's current water rates consist of separate declining block rate schedules for 5/8-inch, 1-inch, 1 1/4-inch, 1 1/2-inch and 2-inch meters and a field connection schedule, containing from 2 to 4 rate steps.

Boonesboro proposed to change its rate design by eliminating the 1 1/4-inch meter schedule and reducing the rate steps in the remaining schedules. The minimum usage would remain the same, and minimum bills for each meter size would equal the amount the minimum usage would cost when calculated under the 5/8-inch meter rates. All usage in excess of the minimum would be billed at the same rate per 1,000 gallons regardless of meter size.

In its response to the Commission's order of July 26, 1985, Boonesboro stated that the contract for purchased water limits the volume of water which can be purchased from its supplier, thus,

creating a need to encourage conservation especially by its large industrial users through a change in its rate structure. Boonesboro does not have an alternate source of supply. The proposed rate design would also result in all customers paying the same rate per gallon regardless of the volume used.

The Commission is of the opinion that the change in water rate design proposed by Boonesboro is an appropriate conservation measure and, further, that the equalization of rates is fair, just and reasonable. The proposed change in the water rate design should be approved.

Fire Hydrant Rate

Boonesboro currently has a separate fire hydrant rate schedule consisting of a connection fee plus a yearly water usage rental rate. Boonesboro proposed to change the fire hydrant rate design so that a flat fee of \$500 would be charged to the owner or occupant of a premises each time a fire hydrant was used for fire fighting purposes for that premises.

In its response, filed September 18, 1985, and testimony of Mr. David Haggard, a contractor for the utility,¹⁰ Boonesboro stated it had no way to determine the amount of water used in fighting a fire, but estimated 100,000 gallons would be used over a period of 2 or 3 hours. The \$500 amount was chosen for the following reasons: (1) It was felt that was the maximum most insurance companies would pay under homeowners insurance; (2) Boonesboro wanted the rate high enough so it would average out to

¹⁰ T.E., October 24, 1985, pages 98-101.

provide reimbursement for a small fire or a large fire; and (3) it was felt the high rate would discourage illegal use of water from the fire hydrants.

Boonesboro does not know how many fire hydrants it has and no revenue was collected from the current rates during the test year. Maintenance of the fire hydrants is paid through the general rates. Boonesboro does not plan to coordinate with the fire department in assessing the proposed charge.

No evidence was provided to show that payment for water used in fire fighting would be covered by an insurance company, nor was any evidence provided upon which a reasonable estimate of the average amount of water used for fire fighting could be based. Under the current rate schedule, \$500 would pay for approximately 350,000 gallons of water and under the rates granted herein approximately 274,000 gallons, substantially more than the amount which would be used in a 2 or 3 hour period.

Further, no evidence was presented to show how this charge would discourage illegal use of water. In addition to the difficulty in identifying both the illegal use and the user, if such person or persons are not deterred by the legal sanctions which may result from their actions, it is highly unlikely they will be deterred by a fire hydrant user fee.

The Commission is of the opinion that the reason given for this rate, the amount, and the method of application presented by Boonesboro do not provide adequate justification and that it should, therefore, be denied.

Sewer Rates

Boonesboro's current charge for sewer service is 50 percent of the water bill. It proposed to increase the charge to 60 percent of the water bill. In support of this method of charging for sewer service, Boonesboro stated in its September 18, 1985, response that it assumes all water used by its customers will be treated by the sewer plant, and the greater the water usage the greater the share of expense borne by the customer toward the expense of operating the sewer plant. It also felt a flat rate would be difficult to administer and would treat lesser water users unfairly. Very little evidence was presented as to the cost of sewer operations or in support of the assumption that all water used is treated by the sewer plant. The method of billing used by Boonesboro is unfair, unjust and unreasonable in that it allows for an automatic increase in sewer rates whenever water rates are increased without a vehicle for review and justification of such increase. In addition, the table showing water used by sewer customers, filed with the response of November 20, 1985, shows that 729 of the 773 bills rendered for sewer service during the test year were for 5/8-inch meter customers. Of these, 453 used 3,500 gallons of water or less which would represent a maximum sewer bill of \$6.41. In any utility rate, there are certain fixed expenses incurred for every customer regardless of usage. The current rate structure is not adequate to insure that such fixed costs are fairly allocated or to insure that proper consideration is given to sewer plant operations and expenses. The Commission

is of the opinion, therefore, that a separate rate should be established for sewer service.

Tap Fees

Boonesboro proposed to adjust its tap fees to more closely reflect the cost and has provided cost justification for each size meter. The Commission is of the opinion that the proposed tap fees are reasonable and should be approved.

Other Charges

Boonesboro proposed to establish an initiation of service fee to be charged subsequent customers at a location after service to the initial customer at that location is terminated. This charge would also be made when service is reconnected after termination of service for non-payment of bills. Boonesboro further, proposed to establish a charge for changing or testing a meter upon request by a customer. Where a meter test is involved, the charge would apply only where the meter accuracy is outside the limits prescribed by the Commission's regulations, and the meter has been tested within the periodic test interval required by 807 KAR 5:066(7). Special charges were also proposed for reading a meter a second time at the customer's request when the second reading confirms the first, and also for returned checks. The Commission is of the opinion that these are fair, just and reasonable charges to specific customers for whom the cost is incurred.

Boonesboro proposed to charge interest of 2 percent per month in addition to a 10 percent late payment penalty on all bills not paid by the end of the month in which the bill was

rendered. The purpose of the late payment penalty is to provide an incentive for prompt payment as well as to recover some costs of additional billing. The Commission's regulations and the special charges proposed by Boonesboro herein allow for recovery of costs resulting from non-payment of bills. Interest on unpaid bills may not be charged in addition thereto.

Boonesboro proposed to require a deposit not to exceed 2/12 of the estimated annual bill or \$75 whichever is greater. 807 KAR 5:006, Section 7, allows a utility to either require 2/12 of the estimated annual bill or to establish a flat deposit for all customers in the same class; however, a flat deposit may not exceed 2/12 of any customer's estimated annual bill and must be the same for all customers in the same class. The utility may choose either option, but must apply the deposit policy uniformly.

Tariff Provisions

In addition to the above, numerous sections of the proposed rules and regulations are not in compliance with Commission regulations and policies. The Commission is of the opinion that, due to the complexity of setting forth the details of such non-compliance herein, the rules and regulations should be addressed by separate Order.

FINDINGS AND ORDERS

The Commission, after consideration of the application and evidence of record and being advised, is of the opinion and finds that:

1. The change in water rate design proposed by Boonesboro is fair, just, and reasonable and should be approved.

2. Sewer rates based on a percentage of the water bill are unfair, unjust and unreasonable. A separate rate schedule should be established for sewer service.

3. The rates for water service proposed by Boonesboro should be denied upon application of KRS 278.030 in that they will produce revenues in excess of that found reasonable herein.

4. The fire hydrant rate proposed by Boonesboro should be denied for the reasons specified herein.

5. The tap fees, meter test charge, meter reading charge, returned check charge, and initiation of service fee are reasonable and should be approved.

6. The deposit requirement proposed by Boonesboro should be denied and, further, Boonesboro should revise its deposit policy as discussed more fully above.

7. The rates and charges in Appendix A are fair, just and reasonable rates for Boonesboro in that they will produce annual operating revenues of approximately \$248,832 for Boonesboro Water and \$11,509 for Boonesboro Sewer. These revenues will be sufficient to meet Boonesboro's operating expenses for both utilities, service its debt, and provide a reasonable surplus.

IT IS THEREFORE ORDERED THAT:

1. The water and sewer rates proposed by Boonesboro be and they hereby are denied.

2. The fire hydrant rate proposed by Boonesboro be and it hereby is denied.

3. The deposit policy proposed by Boonesboro be and it hereby is denied.

4. The rules and regulations other than those specifically approved or denied herein shall be addressed by separate Order.


5. The tap fees, meter test charge, meter reading charge, initiation of service fee, and returned check charge be and they hereby are approved.

6. The rates and charges in Appendix A be and they hereby are approved for service rendered by Boonesboro on and after the date of this Order.

7. Within 30 days from the date of this Order Boonesboro shall file with this Commission its revised tariff sheets setting out the rates approved herein.

Done at Frankfort, Kentucky, this 9th day of December, 1985.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:

Secretary

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 9312 DATED 12/9/85

The following rates and charges are prescribed for the customers in the area served by Boonesboro Water Association, Inc. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the effective date of this Order.

WATER RATES

5/8-Inch Meter

<u>Usage Level</u>	<u>Monthly Rate</u>
First 1,000 gallons	\$9.00 Minimum
Over 1,000 gallons	1.80 per 1,000 gallons

1-Inch Meter

First 10,000 gallons	\$25.20 Minimum
Over 10,000 gallons	1.80 per 1,000 gallons

1 1/2-Inch Meter

First 30,000 gallons	\$61.20 Minimum
Over 30,000 gallons	1.80 per 1,000 gallons

2-Inch Meter

First 50,000 gallons	\$97.20 Minimum
Over 50,000 gallons	1.80 per 1,000 gallons

SEWER RATES

	<u>Monthly Rate</u>
First 12,000 gallons of water used	\$11.25 Minimum
All usage in excess of 12,000 gallons	11.25 residential equivalent*

- * Residential equivalents or fractions thereof shall be determined by dividing the customers monthly water usage by 12,000 gallons. The minimum bill for the first 12,000 gallons shall be \$11.25 with each additional 12,000 gallon or fraction thereof considered as a residential equivalent.

TAP FEES

Meter Size

5/8-Inch	\$400
1-Inch	500
1 1/2 Inch	900
2-Inch	1,100
Fire Hydrant Connection Charge	\$200
Initiation of Service	25
Returned Check Charge	10
Meter Test or Meter Change	50
Meter Reading	10